

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 19797
[REDACTED])	
)	DECISION
Petitioners.)	
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[Redacted] (petitioners) protest the Notice of Deficiency Determination issued by the auditor for the Idaho State Tax Commission (Commission) dated August 30, 2006. The Notice of Deficiency Determination asserted additional liabilities for Idaho income tax and interest in the total amounts of \$7,456 and \$4,938 for 2004 and 2005, respectively.

The petitioners claimed a theft loss from the loss of their investment account to a "Ponzi scheme." They computed a net operating loss (including the "Ponzi scheme" loss) and carried it to their 2004 and 2005 Idaho income tax returns. The auditor disallowed the net operating loss carried forward by the petitioners. For two reasons, we find the auditor's determination must be affirmed.

The question before us is governed by Idaho Code § 63-3021 which stated, in pertinent part:

Net operating loss. -- (a) The term "net operating loss" means the amount by which Idaho taxable income, after making the modifications specified in subsection (b) of this section, is less than zero.

(b) Add the following amounts:

(1) The amount of any net operating loss deduction included in Idaho taxable income.

(2) In the case of a taxpayer other than a corporation:

(i) Any amount deducted due to losses in excess of gains from sales or exchanges of capital assets; and

(ii) Any deduction for long-term capital gains provided by this chapter.

(3) Any deduction allowed under section 151 of the Internal Revenue Code (relating to personal exemption) or any deduction in lieu of any such deduction.

(4) Any deduction for the standard or itemized deductions provided for in section 63 of the Internal Revenue Code, or section 63-3022(j), Idaho Code, except for any deduction allowable under section 165(c)(3) of the Internal Revenue Code (relating to casualty losses) pertaining to property physically located inside Idaho at the time of the casualty. (Underlining added.)

The “Ponzi-scheme” loss was claimed as an itemized deduction. Therefore, unless this deduction is allowable under section 165(c)(3) of the Internal Revenue Code, it is to be excluded from the computation of the net operating loss. Internal Revenue Code § 165 states, in part:

Losses.

(a) General rule.

There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(b) Amount of deduction. For purposes of subsection (a), the basis for determining the amount of the deduction for any loss shall be the adjusted basis provided in section 1011 for determining the loss from the sale or other disposition of property.

(c) Limitation on losses of individuals. In the case of an individual, the deduction under subsection (a) shall be limited to

(1) losses incurred in a trade or business;

(2) losses incurred in any transaction entered into for profit, though not connected with a trade or business; and

(3) except as provided in subsection (h), losses of property not connected with a trade or business or a transaction entered into for profit, if such losses arise from fire, storm, shipwreck, or other casualty, or from theft.

The allowance of those losses addressed by Internal Revenue Code § 165(c)(3), but not those addressed by § 165(c)(1) (relating to business losses) or § 165(c)(2) (relating to transactions entered into for profit) favors the losses from personal losses over losses from

business endeavors or transactions entered into for profit. The loss in question in this docket would fall under § 165(c)(2) and therefore would not be includable in the computation of an Idaho net operating loss pursuant to Idaho Code § 63-3021.

The second reason that the auditor is correct is due to the nature of the item from which the loss has arisen. The property must have been “physically located inside Idaho at the time of the casualty.” The investment is an intangible. The U. S. Supreme Court has held that “intangible property is not physical matter which can be located on a map.” Delaware v. New York, 507 U.S. 490, 498 (1993); Texas v. New Jersey, 379 U.S. 674, 677 (1965). If it cannot be located on a map, it follows that it cannot be “physically located inside Idaho at the time of the casualty.”

The result reached herein may seem illogical or may not seem to be socially or economically sound. Such an argument was addressed by the Idaho Supreme Court as follows:

The Stangs urge this Court to "construe" the Idaho Income Tax Code in a manner that would permit the Stangs to avoid paying Idaho income tax on the \$8,000 distribution. They argue that because the Idaho Income Tax Code does not expressly address this situation, this Court should be free to construe the tax code in a manner that would prevent the Stangs from having to pay taxes to both California and Idaho on the same monies. When construing the provisions of the Idaho Income Tax Code, however, we must enforce the law as written. Potlatch Corp. v. Idaho State Tax Comm'n, 128 Idaho 387, 913 P.2d 1157 (1996). If there is any ambiguity in the law concerning tax deductions, the law is to be construed strongly against the taxpayer. *Id.* This Court has no authority to rewrite the tax code. Bogner v. State Dep't of Revenue and Taxation, 107 Idaho 854, 693 P.2d 1056 (1984). Any exemption from taxation must be created or conferred in clear and plain language and cannot be made out by inference or implication. Herndon v. West, 87 Idaho 335, 393 P.2d 35 (1964). This Court does not have the authority to create deductions, exemptions, or tax credits. If the provisions of the tax code are socially or economically unsound, the power to correct it is legislative, not judicial. *Id.*

Idaho State Tax Commission v. Stang, 135 Idaho 800, 802-803 (2001).

The petitioner has made logical arguments that the auditor's position should not be affirmed. However, the Commission finds that the law is clear as written and therefore does not lend itself to constructive arguments. The Idaho Supreme Court has addressed this issue as follows:

The clearly expressed intent of our legislature must be given effect and there is no occasion for construction where language of the statute is unambiguous. Ottesen ex rel. Edwards v. Board of Commr's of Madison County, 107 Idaho 1099, 695 P.2d 1238 (1985). In construing a statute, the words of the statute must be given their plain, usual and ordinary meaning. Walker v. Hensley Trucking, 107 Idaho 572, 691 P.2d 1187 (1984); State v. Moore, 111 Idaho 854, 727 P.2d 1282 (Ct.App.1986).

Sherwood v. Carter, 119 Idaho 246, 254 (1991).

Since the Commission has found that the law is clear and that it does not provide for the deduction sought by the petitioners, the auditor's position must be affirmed.

WHEREFORE, the Notice of Deficiency Determination dated August 30, 2006 is hereby APPROVED, AFFIRMED, AND MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the petitioners pay the following tax and interest (computed to April 30, 2007):

<u>YEAR</u>	<u>TAX</u>	<u>INTEREST</u>	<u>TOTAL</u>
2004	\$6,808	\$857	\$ 7,665
2005	4,772	314	<u>5,086</u>
		TOTAL DUE	<u>\$12,751</u>

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the petitioners' right to appeal this decision is enclosed with this decision.

DATED this ____ day of _____, 2007.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2007, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[REDACTED]

Receipt No.

[REDACTED]